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Do cross-border mergers and acquisitions increase short-term market performance? The case of Chinese firms

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ABSTRACT

Despite the new momentum in cross-border mergers and acquisitions (M&As) by emerging market firms, we have a limited understanding of the impact of these activities. Drawing on signalling theory and the institution-based view, this paper examines the extent of stock market reactions to the announcement of cross-border M&A deals, based on an event study of a sample of Chinese firms during the period 2000–2012. The findings indicate that the announcement of cross-border M&As results in a positive stock market reaction; this effect is more significant in the mainland Chinese stock markets (Shanghai and Shenzhen) than that in the Hong Kong market. The shareholders of Chinese firms that acquire a target firm in a host country with a low level of political risk gain higher cumulative abnormal returns than those firms targeting companies in countries with a high level of political risk. The shareholders of Chinese state-owned enterprises experience lower abnormal returns compared with those of Chinese privately owned firms when engaging in cross-border M&A deals.

1. Introduction

Emerging-economy (EE) firms have increasingly used cross-border mergers and acquisitions (M&As) as their internationalization strategy in recent years. For example, Chinese firms have been actively involved in cross-border M&As due to the 'Go Out Policy' (Chen, 2008a, 2008b) implemented by the Chinese government. The number of completed cross-border M&As by Chinese firms was only 33 in 2000 and the total value of these deals was $838.86 million dollars, whereas in 2012 the number of completed deals increased to 146 and their value reached $22.32 billion dollars (Thomson One Banker, 2013). Chinese firms have attracted attention worldwide with a series of high-profile cross-border M&As involving well-known western companies, including Lenovo's acquisition of the Motorola Mobility division (2014) and IBM's PC division (2005), Geely's acquisition of Volvo Corporation (2010), Wanda's acquisition of Sunseeker (2013) and the AMC Cinema chain (2012), and Huawei's acquisition of Symantec (2011) and CIP (2012). No wonder that the Economist (2010) noted that 'China buys up the world'.

Despite the rapid pace and increasing importance of cross-border M&As by Chinese firms, existing research has predominantly focused on M&As undertaken by firms from developed countries (Ghosh, 2001; Kruse, Park, Park, & Suzuki, 2007; Martynova & Renneboog, 2008; Pazarskis, Vogiatzogloy, Christodoulou, & Drogalas, 2006; Sharma & Ho, 2002). Only recently have a growing number of studies begun to examine cross-border M&As by EE firms (Buckley, Elia, & Kafouros, 2014; Deng & Yang, 2015; Lebedev, Peng, Xie, & Stevens, 2015; Ning, Kuo, Strange, & Wang, 2014; Sun, Peng, Ren, & Yan, 2012). Some of these studies (Bhagat, Malhotra, & Zhu, 2011; Boateng, Wang, & Yang, 2008; Wang & Boateng, 2007; Zhou, Guo, Hua, & Doukas, 2015) found a positive market reaction to cross-border M&As, while others (Aybar & Ficici, 2009; Chen & Young, 2010) found a negative one. The inconsistent findings of the existing studies suggest that stock market reactions to cross-border M&As by Chinese firms need further academic scrutiny.

In addition, existing research has tended to assume that there are the same market reactions across stock markets in mainland China and Hong Kong. However, under the formula of 'one country, two systems' (China.org.cn, 2008), the Hong Kong stock market is different from those of mainland China. This leads to a 'one country, two markets' scenario, thus demonstrating the unique institutional setting of China's stock markets. The different institutional arrangements (e.g. ownership restrictions, currency control and liquidity restrictions) between the two markets within one country may trigger different market reactions to the

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announcement of cross-border M&As by Chinese firms. This unique 'one country, two markets' scenario remains underexplored in the domain of cross-border M&As.

Furthermore, there is a lack of comprehensive studies to investigate whether the level of political risk in target countries, and the ownership status of acquiring firms, spur different market reactions to cross-border M&A deals. The stock market is sensitive to any political risk associated with cross-border M&As, which is considered as an important signal, especially in emerging economies (Chan and Wei, 1996; Kim and Mei, 2001; Wang, Liu, & Wang, 2004). However, existing studies tend to focus on the impact of geographic and cultural distance on cross-border M&As (Chakrabarti & Mitchell, 2013; Ragozzino, 2009) without explicitly taking political risk into account. A recent study by Harzing and Pudelko (2016) has shown that cultural distance is often used as a proxy for political risk and government restrictions in a host country, and calls for more studies that use more appropriate and accurate constructs to measure host country characteristics, such as political risk. In addition to political risk, we have a limited understanding of how the ownership status of Chinese acquiring firms affects investors' perception, and hence stock market reactions.

To remedy these research gaps, we examine the following research questions. What are the stock market reactions to cross-

Table 1
A summary of existing studies on the link between cross-border M&As and stock market performance.

Market	Author(s), (year)	Sample period	Details of Sample	Findings
Panel A: developed markets				
US	Dodd (1980)	1970–1977	151 takeovers	−0.23% cumulative abnormal return on the announcement date from completed bids
US	Bradley, Desai, and Kim (1983)	1962–1980	241 successful deals, 94 unsuccessful deals	−0.64% insignificant returns for the unsuccessful bidders over −20 and +20 days period
US	Lang et al. (1989)	1968–1986	87 targets and bidders from successful tender offers	Negative impact on bidder returns when the bid is made by a firm with a low Tobin's *q*
US	Smith and Kim (1994)	1980–1986	177 bidders and targets	0.23% significant abnormal returns over −1 and 0 days
US	Floreani and Rigamonti (2001)	1996–2000	56 listed acquirers	3.65%.abnormal returns obtained by insurance companies
US	Song and Walking (2004)	1985–2001	5726 mergers and acquisitions	Acquiring firms with a period of more than one year of 'dormant' bid activity receive a positive abnormal return of 0.8%. Acquirers with a 'dormant' period of less than one year earn insignificant returns
US	Faccio et al. (2006)	1996–2001	4429 acquirers of listed and unlisted targets	−0.38% significant abnormal returns for acquirers of unlisted targets, while 1.48% significant abnormal returns for acquirers
US	Masulis et al. (2007)	1990–2003	3333 completed acquisitions	Acquires operating in more competitive industries or separating the positions of CEO and chairman of the board experience higher abnormal announcement returns
UK	Holl and Kyriazis (1997)	1979–1989	178 successful bids	−1.25% significantly negative abnormal returns for bidders over the two months after the bid announcement
UK	Sudarsanam and Mahate (2003)	1983–1995	519 listed acquirers	between −1.39% and −1.47% significantly negative abnormal returns for UK acquirers
UK	Conn, Cosh, Guest, and Hughes (2005)	1984–1998	4344 acquisitions	Significantly positive announcement returns for bidders when the culture difference is great between U.K. bidders firms and foreign target firms
UK	Gregory and McCorriston (2005)	1985–1994	343 acquisitions	Short-run returns are insignificantly different from zero irrespective of the location of the acquisition
EU	Campa and Hernando (2004)	1998–2000	262 mergers and acquisitions	−1.96% negative abnormal returns for regulated EU acquirers over 60 days around the bid announcement. No significant returns for bidders from unregulated industries for the same period
EU	Goergen and Renneboog (2004)	1993–2000	187 bidders	1.2% significantly cumulative abnormal returns for bidders over 5 days around the announcement date
EU	Chari et al. (2010)	1986–2006	594 acquisitions in emerging markets and 1624 acquisitions in developed markets	1.16% significantly positive abnormal returns for developed-marker acquirers over a three-day event window
Canada	Ben-Amar and Andre (2006)	1998–2000	238 mergers and acquisitions by 138 Canadian firms	1.6% abnormal returns for acquiring firms over 3 days
Canada	Dutta, Saadi, and Zhu (2013)	1993–2002	1300 completed acquisitions	Significantly positive abnormal returns for Canadian acquiring firms' shares around the announcement date
Panel B: emerging market				
India	Gubbi et al. (2010)	2000–2007	425 cross-border acquisitions by Indian firms	International acquisitions by Indian firms earn significantly positive value for their shareholders
India and China	Nicholson and Salaber (2013)	2000–2010	203 Indian and 63 Chinese cross-border deals	Cross-border acquisitions made by Indian and Chinese firms lead to significant shareholder wealth creation. Indian shareholders are more likely to benefit from deals in small culture distance countries, While Chinese investors gain from cross-border expansion of manufacturing companies
China	Chen and Young (2010)	2000–2008	39 deals by 32 Chinese MNEs	Negative average cumulated abnormal returns for Chinese acquiring MNEs
China	Ning et al. (2014)	1991–2010	335 acquisitions	Significant positive shareholder value for Chinese acquiring MNEs
Emerging market	Aybar and Ficici (2009)	1991–2004	433 acquisitions by 58 emerging-market multinationals	The equity markets react negatively to the emerging market cross-border acquisition announcement
Emerging market	Bhagat et al. (2011)	1991–2008	698 acquisitions by publicly listed firms from eight emerging countries	Emerging country acquirers experience a positive and significant market response of 1.09% on the announcement day

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